

Edgar Filing: Home Federal Bancorp, Inc. - Form 10-Q

Home Federal Bancorp, Inc.  
Form 10-Q  
February 06, 2009  
UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended December 31, 2008

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 000-52995

HOME FEDERAL BANCORP, INC.  
(Exact name of registrant as specified in its charter)

Maryland  
(State or other jurisdiction of incorporation or organization)

68-0666697  
(I.R.S. Employer I.D. Number)

500 12th Avenue South, Nampa, Idaho  
(Address of principal executive offices)

83651  
(Zip Code)

Registrant's telephone number, including area code: (208) 466-4634

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer   
Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: Common Stock, \$.01 par value per share, 17,383,931 shares outstanding as of February 2, 2009.

---

HOME FEDERAL BANCORP, INC.  
FORM 10-Q  
TABLE OF CONTENTS

PART  
1 - FINANCIAL INFORMATION

|          |  |      |
|----------|--|------|
| Item 1 - | Financial Statements   | Page |
|          | Consolidated Balance Sheets as of<br>December 31, 2008 and September 30, 2008  | 1    |
|          | Consolidated Statements of Income for the Three Months<br>ended December 31, 2008 and 2007   | 2    |
|          | Consolidated Statements of Changes in Stockholders' Equity and<br>Comprehensive Income for the Three Months<br>ended December 31, 2008 | 3    |
|          | Consolidated Statements of Cash Flows for the Three Months<br>ended December 31, 2008 and 2007   | 4    |
|          | Selected Notes to Interim Consolidated Financial Statements  | 5    |
| Item 2 - | Management's Discussion and Analysis of Financial Condition<br>and Results of Operations   | 12   |
| Item 3 - | Quantitative and Qualitative Disclosures About Market Risk   | 24   |
| Item 4 - | Controls and Procedures  | 25   |

PART  
II - OTHER INFORMATION

|           |   |    |
|-----------|---|----|
| Item 1 -  | Legal Proceedings   | 25 |
| Item 1A - | Risk Factors  | 25 |
| Item 2 -  | Unregistered Sales of Equity Securities and Use of Proceeds | 26 |
| Item 3 -  | Defaults Upon Senior Securities                             | 26 |
| Item 4 -  | Submission of Matters to a Vote of Security Holders         | 26 |
| Item 5 -  | Other Information   | 27 |
| Item 6 -  | Exhibits  | 27 |

SIGNATURES

28



## Item 1. Financial Statements

| HOME FEDERAL BANCORP, INC. AND SUBSIDIARY<br>CONSOLIDATED BALANCE SHEETS<br>(In thousands, except share data) (Unaudited) | December<br>31,<br>2008 | September<br>30,<br>2008 |
|---|-------------------------|--------------------------|
| <b>ASSETS</b>   |                         |                          |
| Cash and amounts due from depository institutions   | \$ 17,412               | \$ 23,270                |
| Certificate of deposit in correspondent bank  | -                       | 5,000                    |
| Mortgage-backed securities available for sale, at fair value  | 188,237                 | 188,787                  |
| Federal Home Loan Bank of Seattle ("FHLB") stock, at cost   | 9,591                   | 9,591                    |
| Loans receivable, net of allowance for loan losses of \$8,027<br>and \$4,579  | 466,169                 | 459,813                  |
| Loans held for sale   | 2,267                   | 2,831                    |
| Accrued interest receivable   | 2,534                   | 2,681                    |
| Property and equipment, net   | 16,073                  | 15,246                   |
| Mortgage servicing rights, net  | -                       | 1,707                    |
| Bank owned life insurance   | 11,696                  | 11,590                   |
| Real estate and other property owned  | 1,352                   | 650                      |
| Deferred tax asset  | -                       | 1,770                    |
| Other assets  | 2,802                   | 2,134                    |
| <b>TOTAL ASSETS</b>   | <b>\$718,133</b>        | <b>\$725,070</b>         |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                         |                          |
| <b>LIABILITIES</b>  |                         |                          |
| Deposit accounts:   |                         |                          |
| Noninterest-bearing demand deposits   | \$ 41,187               | \$ 41,398                |
| Interest-bearing demand deposits  | 134,148                 | 127,714                  |
| Savings deposits  | 27,589                  | 26,409                   |
| Certificates of deposit   | 174,475                 | 177,404                  |
| Total deposit accounts  | 377,399                 | 372,925                  |
| Advances by borrowers for taxes and insurance   | 721                     | 1,386                    |
| Interest payable  | 486                     | 552                      |
| Deferred compensation   | 5,230                   | 5,191                    |
| FHLB advances   | 124,574                 | 136,972                  |
| Deferred tax liability, net   | 310                     | -                        |
| Other liabilities   | 1,965                   | 2,857                    |
| <b>Total liabilities</b>  | <b>510,685</b>          | <b>519,883</b>           |
| <b>STOCKHOLDERS' EQUITY</b>   |                         |                          |
| Serial preferred stock, \$.01 par value; 10,000,000 authorized,<br>issued and outstanding, none                           | --                      | --                       |
| Common stock, \$.01 par value; 90,000,000 authorized,<br>issued and outstanding:  | 174                     | 174                      |
| Dec. 31, 2008 – 17,445,311 issued, 17,392,289 outstanding   |                         |                          |
| Sept. 30, 2008 – 17,412,449 issued, 17,374,161 outstanding  |                         |                          |
| Additional paid-in capital  | 157,813                 | 157,205                  |
| Retained earnings   | 58,118                  | 59,813                   |

Edgar Filing: Home Federal Bancorp, Inc. - Form 10-Q

|  |                  |                  |
|--|------------------|------------------|
| Unearned shares issued to employee stock ownership plan ("ESOP") | (10,378)         | (10,605)         |
| Accumulated other comprehensive income (loss)                    | 1,721            | (1,400)          |
| Total stockholders' equity                                       | 207,448          | 205,187          |
| <b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>                | <b>\$718,133</b> | <b>\$725,070</b> |

See accompanying notes

---

1

HOME FEDERAL BANCORP, INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF INCOME

(In thousands, except share data) (Unaudited)

|   | Three Months Ended<br>December 31, |               |
|---|------------------------------------|---------------|
|   | 2008                               | 2007          |
| Interest and dividend income:                                 |                                    |               |
| Loan interest   | \$ 7,113                           | \$ 8,076      |
| Investment interest   | 43                                 | 264           |
| Mortgage-backed security interest                             | 2,205                              | 1,943         |
| FHLB dividends  | (33)                               | 19            |
| Total interest and dividend income                            | 9,328                              | 10,302        |
| Interest expense:   |                                    |               |
| Deposits  | 2,018                              | 3,214         |
| FHLB advances   | 1,565                              | 2,032         |
| Total interest expense  | 3,583                              | 5,246         |
| Net interest income   | 5,745                              | 5,056         |
| Provision for loan losses                                     | 3,575                              | 287           |
| Net interest income after provision for loan losses           | 2,170                              | 4,769         |
| Noninterest income:   |                                    |               |
| Service charges and fees                                      | 2,109                              | 2,232         |
| Gain on sale of loans   | 190                                | 185           |
| Increase in cash surrender value of bank owned life insurance | 106                                | 104           |
| Loan servicing fees   | 69                                 | 127           |
| Mortgage servicing rights, net                                | (31)                               | (68)          |
| Other   | 18                                 | 45            |
| Total noninterest income                                      | 2,461                              | 2,625         |
| Noninterest expense:  |                                    |               |
| Compensation and benefits                                     | 3,575                              | 3,699         |
| Occupancy and equipment                                       | 770                                | 711           |
| Data processing   | 542                                | 522           |
| Advertising   | 248                                | 287           |
| Postage and supplies  | 137                                | 150           |
| Professional services   | 335                                | 212           |
| Insurance and taxes   | 155                                | 85            |
| Other   | 272                                | 217           |
| Total noninterest expense                                     | 6,034                              | 5,883         |
| Income (loss) before income taxes                             | (1,403)                            | 1,511         |
| Income tax expense (benefit)                                  | (602)                              | 564           |
| NET INCOME (LOSS)   | \$ (801)                           | \$ 947        |
| Earnings (loss) per share:                                    |                                    |               |
| Basic   | \$(0.05)                           | \$0.06(1)     |
| Diluted   | (0.05)                             | 0.06(1)       |
| Weighted average number of shares outstanding:                |                                    |               |
| Basic   | 16,129,352                         | 16,738,289(1) |
| Diluted   | 16,129,352                         | 16,762,906(1) |
| Dividends declared per share:                                 | \$0.055                            | \$0.048(1)    |

(1) Earnings per share, average shares outstanding, and dividends per share have been adjusted to reflect the impact of the second-step conversion and reorganization of Home Federal Bancorp, Inc., which occurred on December 19, 2007.

See accompanying notes.

---

2



HOME FEDERAL BANCORP, INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY AND COMPREHENSIVE  
INCOME

(In thousands, except share data) (Unaudited)

|  | Common Stock |        |                            | Retained Earnings | Unearned Shares Issued to Employee Stock Ownership Plan | Accumulated Other Comprehensive Loss | Total     |
|--|--------------|--------|----------------------------|-------------------|---|--------------------------------------|-----------|
|  | Shares       | Amount | Additional Paid-In Capital |                   |   |                                      |           |
| Balance at Sept. 30, 2007  | 15,232,243   | \$152  | \$ 59,613                  | \$58,795          | \$ (3,698)  | \$(2,225)                            | \$112,637 |
| Second Step Conversion(1)  | 2,073,619    | 21     | 95,938                     |                   | (8,160)   |                                      | 87,799    |
| Dissolution of Mutual Holding Company  |              |        | 50                         |                   |   |                                      | 50        |
| Restricted stock issued, net of forfeitures                                      | 13,502       |        |                            |                   |   |                                      | --        |
| ESOP shares committed to be released   |              |        | (23)                       |                   | 1,253   |                                      | 1,230     |
| Exercise of stock options  | 54,797       |        | 1 605                      |                   |   |                                      | 606       |
| Share-based compensation   |              |        | 1,022                      |                   |   |                                      | 1,022     |
| Dividends paid (\$0.213 per share) (2) (3)                                       |              |        |                            | (2,987)           |   |                                      | (2,987)   |
| Comprehensive income:  |              |        |                            |                   |   |                                      |           |
| Net income   |              |        |                            | 4,005             |   |                                      | 4,005     |
| Other comprehensive income:  |              |        |                            |                   |   |                                      |           |
| Change in unrealized holding loss on securities available for sale, net of taxes |              |        |                            |                   |   | 825                                  | 825       |
| Comprehensive income   |              |        |                            |                   |   |                                      | 4,830     |
| Balance at Sept. 30, 2008  | 17,374,161   | 174    | 157,205                    | 59,813            | (10,605)  | (1,400)                              | 205,187   |
| Restricted stock issued, net of forfeitures                                      | (14,734)     |        |                            |                   |   |                                      | -         |
| ESOP shares committed to be released   |              |        | 27                         |                   | 227   |                                      | 254       |
| Exercise of stock options  | 32,862       |        | 353                        |                   |   |                                      | 353       |
| Share-based compensation   |              |        | 228                        |                   |   |                                      | 228       |
| Dividends paid (\$0.055 per share)   |              |        |                            | (894)             |   |                                      | (894)     |
| Comprehensive income:  |              |        |                            |                   |   |                                      |           |
| Net loss   |              |        |                            | (801)             |   |                                      | (801)     |
| Other comprehensive income:  |              |        |                            |                   |   |                                      |           |
| Change in unrealized holding loss on securities available for                    |              |        |                            |                   |   | 3,121                                | 3,121     |

Edgar Filing: Home Federal Bancorp, Inc. - Form 10-Q

|                          |            |       |           |          |            |          |  |           |
|--------------------------|------------|-------|-----------|----------|------------|----------|--|-----------|
| sale, net of taxes       |            |       |           |          |            |          |  |           |
| Comprehensive income     |            |       |           |          |            |          |  | 2,320     |
| Balance at Dec. 31, 2008 | 17,392,289 | \$174 | \$157,813 | \$58,118 | \$(10,378) | \$ 1,721 |  | \$207,448 |

- (1) The total effect on equity accounts from the second-step conversion has changed from the December 31, 2007 reported numbers due to adjustments such as true-up of total new shares issued in relation to conversion once total affect of fractional shares was known, payment of additional expenses related to the second-step conversion, etc.
- (2) Home Federal MHC waived its receipt of dividends on the 8,979,246 shares that it owned.
- (3) Dividends per share have been adjusted to reflect the impact of the second-step conversion of Home Federal Bancorp, Inc., which occurred on December 19, 2007.

See accompanying notes.

---

| HOME FEDERAL BANCORP, INC. AND SUBSIDIARY<br>CONSOLIDATED STATEMENTS OF CASH FLOWS<br>(In thousands) (Unaudited) | Three Months Ended<br>December 31, |          |
|--|------------------------------------|----------|
|  | 2008                               | 2007     |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>   |                                    |          |
| Net income (loss)  | \$ (801)                           | \$ 947   |
| Adjustments to reconcile net income (loss) to cash provided by operating activities:                             |                                    |          |
| Depreciation and amortization  | 442                                | 397      |
| Net amortization (accretion) of premiums and discounts on investments  | 2                                  | (10)     |
| Loss on sale of fixed assets and repossessed assets  | 63                                 | -        |
| ESOP shares committed to be released   | 254                                | 207      |
| Equity compensation expense  | 228                                | 255      |
| Provision for loan losses  | 3,575                              | 287      |
| Accrued deferred compensation expense, net   | 39                                 | 179      |
| Net deferred loan fees   | 171                                | (18)     |
| Net gain on sale of loans  | (190)                              | (185)    |
| Proceeds from sale of loans held for sale  | 10,476                             | 13,895   |
| Originations of loans held for sale  | (9,817)                            | (11,864) |
| Net decrease in value of mortgage servicing rights   | 31                                 | 68       |
| Net increase in value of bank owned life insurance   | (106)                              | (104)    |
| Change in assets and liabilities:  |                                    |          |
| Interest receivable  | 148                                | (212)    |
| Other assets   | (673)                              | 1,110    |
| Interest payable   | (66)                               | (56)     |
| Other liabilities  | (894)                              | (1,153)  |
| Net cash provided by operating activities  | 2,882                              | 3,743    |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>   |                                    |          |
| Proceeds from maturity of mortgage-backed securities available for sale  | 6,215                              | 5,778    |
| Purchases of mortgage-backed securities available for sale   | (465)                              | -        |
| Maturity of investment in certificate of deposit   | 5,000                              | -        |
| Sale of mortgage servicing rights  | 1,676                              |          |
| Purchases of property and equipment  | (1,269)                            | (598)    |
| Net (increase) decrease in loans   | (10,956)                           | 2,099    |
| Proceeds from sale of fixed assets and repossessed assets  | 188                                | 128      |
| Net cash provided by investing activities  | 389                                | 7,407    |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>   |                                    |          |
| Net increase in deposits   | 4,474                              | 363      |
| Net decrease in advances by borrowers for taxes and insurance  | (665)                              | (833)    |
| Proceeds from FHLB advances  | 18,030                             | 5,300    |
| Repayment of FHLB advances   | (30,428)                           | (22,392) |
| Net proceeds from stock issuance and exchange pursuant to second step conversion                                 | -                                  | 88,454   |

Edgar Filing: Home Federal Bancorp, Inc. - Form 10-Q

|  |           |           |
|--|-----------|-----------|
| Proceeds from exercise of stock options                              | 353       | 147       |
| Dividends paid   | (893)     | (324)     |
| Net cash (used) provided by financing activities                     | (9,129)   | 70,715    |
| <br>   |           |           |
| NET (DECREASE) INCREASE IN CASH AND CASH<br>EQUIVALENTS              | (5,858)   | 81,865    |
| CASH AND CASH EQUIVALENTS, BEGINNING OF<br>PERIOD                    | 23,270    | 20,588    |
| CASH AND CASH EQUIVALENTS, END OF PERIOD                             | \$ 17,412 | \$102,453 |
| <br>   |           |           |
| SUPPLEMENTAL DISCLOSURE OF CASH FLOW<br>INFORMATION:                 |           |           |
| Cash paid during the period for:                                     |           |           |
| Interest   | \$3,648   | \$5,302   |
| <br>   |           |           |
| NONCASH INVESTING AND FINANCING ACTIVITIES:                          |           |           |
| Acquisition of real estate and other assets in settlement of loans   | 947       | 312       |
| Fair value adjustment to securities available for sale, net of taxes | 3,121     | 1,522     |

See accompanying notes.

---

HOME FEDERAL BANCORP, INC. AND SUBSIDIARY  
SELECTED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

Note 1 - Basis of Presentation

The consolidated financial statements presented in this quarterly report include the accounts of Home Federal Bancorp, Inc., a Maryland corporation (the “Company”), and its wholly-owned subsidiary, Home Federal Bank (the “Bank”). The financial statements of the Company have been prepared in conformity with accounting principles generally accepted in the United States of America for interim financial information and are unaudited. All significant intercompany transactions and balances have been eliminated. In the opinion of the Company’s management, all adjustments consisting of normal recurring adjustments necessary for a fair presentation of the financial condition and results of operations for the interim periods included herein have been made. Operating results for the three month period ended December 31, 2008, are not necessarily indicative of the results that may be expected for the year ending September 30, 2009.

The Company was formed as the new stock holding company for the Bank in connection with the Bank’s conversion from the mutual holding company structure to the stock holding company structure, which was completed on December 19, 2007 (the “Conversion”). Prior to the completion of the Conversion, the Bank was the subsidiary of Home Federal Bancorp, Inc., a federally-chartered stock mid-tier holding company (“Old Home Federal”), and Old Home Federal was a subsidiary of Home Federal MHC, a federally-chartered mutual holding company. The Bank formed the mutual holding company structure in December 2004. As a result of the Conversion, Home Federal MHC and Old Home Federal ceased to exist and were replaced by the Company as the successor to Old Home Federal. See Note 3 below for additional information regarding the Conversion.

Certain information and note disclosures normally included in the Company’s annual consolidated financial statements have been condensed or omitted. Therefore, these consolidated financial statements and notes thereto should be read in conjunction with the audited financial statements and notes included in the Annual Report on Form 10-K for the year ended September 30, 2008 (“2008 Form 10-K”), filed with the Securities and Exchange Commission (“SEC”) on December 15, 2008.

Note 2 - Critical Accounting Estimates and Related Accounting Policies

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the consolidated financial statements. Changes in these estimates and assumptions are considered reasonably possible and may have a material impact on the consolidated financial statements, and thus actual results could differ from the amounts reported and disclosed herein. The Company considers the allowance for loan losses, and deferred income taxes to be critical accounting estimates.

Allowance for loan losses. The procedures for assessing the adequacy of the allowance for loan losses reflect evaluation of credit risk after careful consideration and interpretation of relevant information. In developing this assessment, management must rely on estimates and exercise judgment regarding matters where the ultimate outcome is unknown such as economic factors, developments affecting companies in specific industries and issues with respect to single borrowers. The allowance for loan losses is maintained at a level that management believes to be the best estimate of probable, incurred losses inherent in the loan portfolio at the balance sheet dates presented. Depending on changes in circumstances, future assessments of credit risk may yield materially different results, which may require an increase or a decrease in the allowance for loan losses.

Deferred income taxes. Deferred income taxes are computed using the asset and liability approach as prescribed in Statement of Financial Accounting Standards (“SFAS”) No. 109, Accounting for Income Taxes. Under this method, a deferred tax asset or liability is determined based on the currently enacted tax rates applicable to the period in which the differences between the financial statement carrying amounts and tax basis of the existing assets and liabilities are expected to be reported in the Company’s income tax returns.

Note 3 –Conversion and Reorganization

The Company is a Maryland corporation that was formed as the new stock holding company for Home Federal Bank in connection with the Conversion. As part of the Conversion, a total of 9,384,000 new shares of the Company were sold at \$10 per share in subscription, community and syndicated community offerings through which the Company received proceeds of approximately \$87.8 million, net of offering costs of approximately \$5.9 million. The Company contributed \$48.0 million, or approximately 50%, of the net proceeds of the offering to the Bank in the form of a capital contribution. The Company loaned \$8.2 million to the Bank's Employee Stock Ownership Plan (the "ESOP") and the ESOP used those funds to acquire 816,000 shares of the Company's common stock at \$10 per share. As part of the Conversion, shares of outstanding common stock of Old Home Federal were exchanged for 1.136 shares of the Company's common stock. No fractional shares were issued. Instead, cash was paid to stockholders at \$10 per share for any fractional shares that would otherwise be issued. The exchange resulted in an additional 852,865 outstanding shares of the Company for a total of 17,325,901 outstanding shares as of the closing of the Conversion on December 19, 2007, after giving effect to the redemption of fractional shares.

The Conversion was accounted for as a reorganization in corporate form with no change in the historical basis of the Company's assets, liabilities and equity. All references to the number of shares outstanding, with the exception of those reported on the Consolidated Balance Sheets, are restated to give retroactive recognition to the exchange ratio applied in the Conversion.

Note 4 – Income Taxes

On October 1, 2007, the Company adopted Financial Accounting Standards Board ("FASB") Interpretation No. 48, Accounting for Uncertainty in Income Taxes ("FIN 48"). FIN 48 requires recognition and measurement of uncertain tax positions using a "more-likely-than-not" approach. The Company's approach to adopting FIN 48 consisted of an examination of its financial statements, its income tax provision, and its federal and state income tax returns. The Company analyzed its tax positions including the permanent and temporary differences as well as the major components of income and expense. As of December 31, 2008, the Company did not believe that it had any uncertain tax positions that would rise to the level of having a material effect on its financial statements. In addition, the Company had no accrued interest or penalties on income tax liabilities as of December 31, 2008. It is the Company's policy to record interest and penalties as a component of income tax expense.

Note 5 - Earnings (Loss) Per Share

Earnings (Loss) per share ("EPS") is computed using the basic and diluted weighted average number of common shares outstanding during the period. Basic EPS is computed by dividing the Company's net income or loss by the weighted average number of common shares outstanding for the period. Diluted EPS is computed by dividing net income or loss by the diluted weighted average shares outstanding, which include common stock equivalent shares outstanding using the treasury stock method, unless such shares are anti-dilutive. Common stock equivalents arise from assumed conversion of outstanding stock options awarded under the Company's 2005 Stock Option and Incentive Plan ("SOP") and from assumed vesting of shares awarded but not released under the Company's 2005 Recognition and Retention Plan ("RRP") plan. ESOP shares are not considered outstanding for earnings per share purposes until they are committed to be released.

The following table presents the computation of basic and diluted EPS for the periods indicated:

|   | Three Months Ended<br>December 31,                 |            |
|---|--|------------|
|   | 2008   | 2007       |
|   | (in thousands, except share<br>and per share data) |            |
| Basic EPS:  |  |            |
| Net income (loss)   | \$ (801)   | \$ 947     |
| Weighted-average common shares<br>outstanding                                 | 16,129,352   | 16,738,289 |
| Basic EPS   | \$ (0.05)  | \$ 0.06    |
| Diluted EPS:  |  |            |
| Net income (loss)   | \$ (801)   | \$ 947     |
| Weighted-average common shares<br>outstanding                                 | 16,129,352   | 16,738,289 |
| Net effect of dilutive RRP awards   | -  | 24,617     |
| Weighted-average common shares<br>outstanding<br>and common stock equivalents | 16,129,352   | 16,762,906 |
| Diluted EPS   | \$ (0.05)  | \$ 0.06    |

During the three months ended December 31, 2008 and 2007, there were 573,544 and 655,240 options excluded from the calculation of EPS as their effect was anti-dilutive.

#### Note 6 - Mortgage-Backed Securities

Mortgage-backed securities available for sale consisted of the following:

| (in thousands)                         | Amortized<br>Cost | December 31, 2008            |                               | Fair<br>Value |
|--|-------------------|------------------------------|-------------------------------|---------------|
|  |                   | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses |               |
| Issued by U.S. Government<br>sponsored |                   |                              |                               |               |
| enterprises                            | \$181,992         | \$3,936                      | \$ (192)                      | \$185,736     |
| Other                                  | 3,376             | -                            | (875)                         | 2,501         |
| Total                                  | \$185,368         | \$3,936                      | \$(1,067)                     | \$188,237     |
| September 30, 2008                     |                   |                              |                               |               |
| Issued by U.S. Government<br>sponsored |                   |                              |                               |               |
| enterprises                            | \$187,730         | \$669                        | \$(2,669)                     | \$185,730     |
| Other                                  | 3,390             | -                            | (333)                         | 3,057         |
| Total                                  | \$191,120         | \$669                        | \$(3,002)                     | \$188,787     |





The fair value of temporarily impaired securities, the amount of unrealized losses and the length of time these unrealized losses existed as of December 31, 2008 were as follows:

|  | Less than 12 months |                   | 12 months or longer |                   | Total      |                   |
|--|---------------------|-------------------|---------------------|-------------------|------------|-------------------|
|  | Fair Value          | Unrealized Losses | Fair Value          | Unrealized Losses | Fair Value | Unrealized Losses |
|  | (in thousands)      |                   |                     |                   |            |                   |
| Mortgage-backed securities, available for sale | \$13,391            | \$(192)           | \$2,502             | \$(875)           | \$15,893   | \$(1,067)         |

Management has evaluated these securities and has determined that the decline in the value is temporary and not related to the underlying credit quality of the issuers. The declines in value are on securities that have contractual maturity dates and, at December 31, 2008, management believes it is reasonably probable that principal and interest balances on those securities will be collected based on the performance, underwriting and vintage of the loans underlying the temporarily-impaired securities. However, continued deteriorating economic conditions may result in degradation in the performance of the loans underlying those securities in the future. The Company has the ability and intent to hold the temporarily-impaired securities for a reasonable period of time for a forecasted recovery of the amortized cost.

As of December 31, 2008, the Bank had pledged mortgage-backed securities with an amortized cost of \$78.2 million and a fair value of \$80.2 million as collateral for FHLB advances. Mortgage-backed securities with an amortized cost of \$5.5 million and a fair value of \$5.7 million at December 31, 2008, were pledged to the Federal Reserve Bank as collateral for treasury tax and loan funds held by the Bank and for borrowings from the discount window. As of September 30, 2008, and December 31, 2008, there was no balance owed by the Company through the Federal Reserve Bank discount window.

## Note 7 - Loans Receivable

Loans receivable are summarized as follows:

|                                 | December 31, 2008 |                  | September 30, 2008 |                  |
|---------------------------------|-------------------|------------------|--------------------|------------------|
|                                 | Balance           | Percent of Total | Balance            | Percent of Total |
| (dollars in thousands)          |                   |                  |                    |                  |
| Real Estate:                    |                   |                  |                    |                  |
| One- to four-family residential | \$203,336         | 42.83%           | \$210,302          | 45.22%           |
| Multi-family residential        | 9,361             | 1.97             | 8,477              | 1.82             |
| Commercial                      | 159,012           | 33.46            | 151,733            | 32.62            |
| Total real estate               | 371,709           | 78.26            | 370,512            | 79.66            |
| Real Estate Construction:       |                   |                  |                    |                  |
| One- to four-family residential | 12,907            | 2.72             | 13,448             | 2.89             |
| Multi-family residential        | -                 | -                | 920                | 0.20             |
| Commercial and land development | 27,340            | 5.75             | 18,674             | 4.01             |
| Total real estate construction  | 40,247            | 8.47             | 33,042             | 7.10             |
| Consumer:                       |                   |                  |                    |                  |
| Home equity                     | 53,743            | 11.31            | 52,954             | 11.38            |
| Automobile                      | 1,750             | 0.37             | 1,903              | 0.41             |
| Other consumer                  | 1,295             | 0.26             | 1,370              | 0.29             |
| Total consumer                  | 56,788            | 11.94            | 56,227             | 12.08            |
| Commercial business             | 6,304             | 1.33             | 5,385              | 1.16             |
|                                 | 475,048           | 100.00%          | 465,166            | 100.00%          |
| Premium on purchased loans      | 197               |                  | 199                |                  |
| Deferred loan fees              | (1,049)           |                  | (973)              |                  |
| Allowance for loan losses       | (8,027)           |                  | (4,579)            |                  |
| Loans receivable, net           | \$466,169         |                  | \$459,813          |                  |

## Note 8 – Mortgage Servicing Rights

On August 28, 2008, Home Federal Bank entered into a binding agreement with another bank whereby the Bank would sell its remaining servicing rights. The purchase price was 1.02% of the unpaid principal balance of all loans in the servicing portfolio, except for those loans that are 60 days or more past due, in litigation, in bankruptcy or in foreclosure as of October 31, 2008. The transfer was completed on December 16, 2008.

The Bank now originates nearly all of its one- to four-family loans for sale in the secondary market with servicing released. As a result, the Bank will not record new capitalized servicing rights.

The following table lists the classes of servicing rights and the activities in the balance of each class for the periods indicated:

| Servicing Right Classes                | Three Months Ended<br>December 31, |         |
|--|------------------------------------|---------|
|  | 2008                               | 2007    |
|  | (in thousands)                     |         |
| One- to four-family residential loans: |                                    |         |
| Beginning Balance                      | \$1,703                            | \$2,033 |
| Adjustments to fair value              | -                                  | (66)    |
| Sale of servicing rights               | (1,703)                            | -       |
| Ending Balance                         | \$ -                               | \$1,967 |
| Commercial real estate loans:          |                                    |         |
| Beginning Balance                      | \$ 4 4                             | \$ 14   |
| Adjustments to fair value              | (4)                                | (2)     |
| Ending Balance                         | \$ -                               | \$ 12   |

The amount of contractually specified servicing fees for one- to four-family residential loans for the three months ended December 31, 2008 and 2007, was \$69,000 and \$127,000, respectively. The amount of contractually specified servicing fees for commercial real estate loans as well as late fees and other ancillary fees earned for the periods indicated were immaterial in amount.

#### Note 9 – Fair Value Measurement

SFAS No. 157 defines fair value, establishes a consistent framework for measuring fair value and expands disclosure requirements about fair value measurements. SFAS No. 157, among other things, requires the Company to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. These two types of inputs create the following fair value hierarchy:

- Level 1 – Quoted prices for identical instruments in active markets.
- Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.
- Level 3 – Instruments whose significant value drivers are unobservable.

The following table summarized the Company's financial instruments that were measured at fair value on a recurring basis at December 31, 2008:

|       | December 31, 2008 |
|-------|-------------------|
| Total | Level 2           |

Edgar Filing: Home Federal Bancorp, Inc. - Form 10-Q

|                                  |           | Level<br>1     |           | Level<br>3 |
|----------------------------------|-----------|----------------|-----------|------------|
|                                  |           | (in thousands) |           |            |
| Securities<br>available for sale | \$188,237 | \$ -           | \$188,237 | \$ -       |

Additionally, certain assets are measured at fair value on a non-recurring basis. These adjustments to fair value generally result from the application of lower-of-cost-or-market accounting or write-downs of individual assets due to impairment. The following table summarizes the Company's financial instruments that were measured at fair value on a non-recurring basis at December 31, 2008:

|                | Total    | December 31, 2008 |       | Level 3  |
|----------------|----------|-------------------|-------|----------|
|                |          | Level             | Level |          |
|                |          | 1                 | 2     |          |
|                |          | (in thousands)    |       |          |
| Impaired loans | \$11,724 | \$ -              | \$ -  | \$11,724 |

Impaired loans which are measured for impairment using the fair value of the collateral at December 31, 2008, had a carrying amount of \$11.7 million, net of valuation allowances totaling \$2.4 million, resulting in an additional provision for loan losses of \$747,000 during the first quarter of fiscal 2009.

The Company used the following methods and significant assumptions to estimate fair value:

**Securities:** The Company's securities available for sale primarily consist of mortgage backed securities issued by U.S. Government sponsored enterprises and trade in active markets. These securities are included under Level 2 because there may or may not be daily trades in each of the individual securities and because the valuation of these securities may be based on instruments that are not exactly identical to those owned by the Company.

**Impaired loans:** A loan is considered impaired when, based upon currently known information, it is deemed probable that the Company will be unable to collect all amounts due as scheduled according to the original terms of the agreement. Impaired loans are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as a practical expedient, based on the loan's observable market price or the fair value of collateral, if the loan is collateral dependent. Impaired loans, which are collateral dependent, are included in the table above.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

### Forward-Looking Statements

This report contains forward-looking statements, which can be identified by the use of words such as "believes," "intends," "expects," "anticipates," "estimates" or similar expressions. Forward-looking statements include, but are not limited to:

- statements of our goals, intentions and expectations;
- statements regarding our business plan, prospects, growth and operating strategies;
  - statements regarding the quality of our loan and investment portfolios; and,
  - estimates of our risks and future costs and benefits.

These forward-looking statements are subject to significant risks and uncertainties. Actual results may differ materially from those contemplated by the forward-looking statements as a result of, among others, the following factors:

- general economic conditions, including real estate values, either nationally or in the Company's market area, that are worse than expected;
- changes in the interest rate environment that reduce the Company's interest margins or reduce the fair value of financial instruments;
- the credit risk of lending activities, including risks related to construction and development lending and commercial and small business banking;
  - changes in the level and trend of loan delinquencies and write-offs;
    - results of examinations by banking regulators;
  - increased competitive pressures among financial services companies;
    - changes in consumer spending, borrowing and savings habits;
  - legislative or regulatory changes that adversely affect the Company's business;
    - adverse changes in the securities markets; and
- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Public Company Accounting Oversight Board or the Financial Accounting Standards Board.

These factors should be considered in evaluating the forward-looking statements, and undue reliance should not be placed on such statements. The Company undertakes no obligation to publish revised forward-looking statements to reflect the occurrence of unanticipated events or circumstances after the date hereof.

### Background and Overview

Home Federal Bank (the "Bank") was founded in 1920 as a building and loan association and reorganized as a federal mutual savings and loan association in 1936. On December 6, 2004, the Bank converted to stock form and reorganized into the two-tiered mutual holding company form of organization and formed Home Federal MHC and Home Federal Bancorp, Inc. ("Old Home Federal"). In connection with that transaction, old Home Federal sold 40.00% of its outstanding shares of common stock (6,083,500 shares) to the public and issued 59.04% of its outstanding shares of common stock (8,979,246 shares) to Home Federal MHC, the mutual holding company parent of Old Home Federal. In connection with that transaction, Old Home Federal also established and capitalized the Home Federal Foundation ("Foundation") for the purpose of supporting charitable organizations and activities that enhance the quality of life for residents within the Bank's market area. The Foundation was capitalized with a \$1.8 million one-time contribution, which consisted of 146,004 shares of its common stock and \$365,010 in cash.



Edgar Filing: Home Federal Bancorp, Inc. - Form 10-Q

On May 11, 2007, the Boards of Directors of Old Home Federal, Home Federal MHC and the Bank adopted a Plan of Conversion and Reorganization (the "Plan") pursuant to which the Bank reorganized from the mutual holding company structure to the stock holding company structure. As a result of that transaction, Home Federal Bank formed a new stock holding company, Home Federal Bancorp, Inc. ("we", "us", the "Company"), that serves as the holding company for Home Federal Bank. Home Federal Bancorp, Inc., is a Maryland corporation. The Conversion was completed on December 19, 2007.

Pursuant to the terms of the Plan, shares of outstanding common stock of Old Home Federal were exchanged for 1.136 shares of the Company's common stock. Cash was paid in lieu of fractional shares. The Conversion was approved by the Bank's members, the Company's stockholders (including the approval of a majority of the shares held by persons other than Home Federal MHC) and regulatory agencies. The Company's common stock is traded on the NASDAQ Global Select Market under the symbol "HOME" and is included in the America's Community Bankers NASDAQ Index and the U.S. Russell 2000® Index.

The Bank is a community-oriented financial institution dedicated to serving the financial service needs of consumers and businesses within its market area. The Bank's primary business is attracting deposits from the general public and using these funds to originate loans. The Bank emphasizes the origination of commercial business loans, commercial real estate loans, construction and residential development loans, consumer loans and loans secured by first mortgages on owner-occupied residential real estate. As a result of a comprehensive and continuing review of its strategic business plan, the Company continues to expand its commercial and small business banking programs, including a variety of loan and deposit products.

The Bank serves the Treasure Valley region of southwestern Idaho, which includes Ada, Canyon, Elmore and Gem counties, through its 15 full-service banking offices and one loan center. Nearly 40% of the state's population lives and works in the four counties served by Home Federal Bank. Ada County has the largest population and includes the city of Boise, the state capital. Home Federal Bank maintains its largest branch presence in Ada County with eight locations, followed by Canyon County with five branches, including the Company's corporate headquarters in Nampa. The two remaining branches are located in Elmore and Gem Counties.

The following items summarize the financial performance of the Company and the key strategic initiatives undertaken by management during the Company's first quarter of fiscal year 2009:

- § A \$3.6 million provision for loan losses contributed to a net loss of (\$801,000), or (\$0.05) per diluted share as economic conditions in the Treasure Valley continued to deteriorate as a result of rising unemployment, bankruptcies and foreclosures and declining real estate values;
- § The Company's efficiency ratio improved to 73.5% for the quarter ended December 31, 2008, compared to 76.6% for the same quarter a year ago;
- § A new banking office was opened in Boise, which was effectively a relocation and upgrade of an older facility;
  - § The Bank broke ground on its sixteenth banking office;
- § Nonperforming and delinquent loans increased significantly as unemployment and real estate pressures continued to increase in the Boise metropolitan statistical area;
  - § The slowdown in consumer spending negatively impacted the Bank's fee income;
- § The Bank began execution of its small business growth strategy by hiring leadership for its newly formed Small Business Banking Group;
  - § The sale of the Bank's mortgage servicing rights asset was completed; and,
  - § The Bank maintained its strong capital position with a total risk-based capital ratio of 31.3% at December 31, 2008.

#### Critical Accounting Estimates and Related Accounting Policies

**Allowance for Loan Losses.** Management recognizes that losses may occur over the life of a loan and that the allowance for loan losses must be maintained at a level necessary to absorb specific losses on impaired loans and probable losses inherent in the loan portfolio. Management assesses the allowance for loan losses on a quarterly basis by analyzing several factors including delinquency rates, charge-off rates and the changing risk profile of the Bank's loan portfolio, as well as local economic conditions such as unemployment rates, bankruptcies and vacancy rates of business and residential properties.

The Company believes that the accounting estimate related to the allowance for loan losses is a critical accounting estimate because it is highly susceptible to change from period to period, requiring management to make assumptions about probable incurred losses inherent in the loan portfolio at the balance sheet date. The impact of a

---

sudden large loss could deplete the allowance and require increased provisions to replenish the allowance, which would negatively affect earnings.

The Company's methodology for analyzing the allowance for loan losses consists of specific allocations on significant individual credits and a general allowance amount, including a range of losses. The specific allowance component is determined when management believes that the collectibility of an individually reviewed loan has been impaired and a loss is probable. The general allowance component relates to assets with no well-defined deficiency or weakness and takes into consideration losses that are inherent within the portfolio but have not been identified. The general allowance is determined by applying a historical loss percentage to various types of loans with similar characteristics and classified loans that are not analyzed specifically. Adjustments are made to historical loss percentages to reflect current economic and internal environmental factors, such as changes in underwriting standards and management turnover, which may increase or decrease those loss factors. As a result of the imprecision in calculating inherent and potential losses, a range is added to the general allowance to provide an allowance for loan losses that is adequate to cover losses that may arise as a result of changing economic conditions and other qualitative factors that may alter historical loss experience. Additionally, future events may evidence additional losses that were unknown at the time management estimated the allowance, which may require an increase in the allowance for loan losses in future periods.

The allowance is increased by the provision for loan losses, which is charged against current period operating results and decreased by the amount of actual loan charge-offs, net of recoveries.

The Company also estimates a reserve related to unfunded loan commitments. In assessing the adequacy of the reserve, the Company uses a similar approach used in the development of the allowance for loan losses. The reserve for unfunded loan commitments is included in other liabilities on the Consolidated Balance Sheets. The provision for unfunded commitments is charged to noninterest expense.

**Deferred Income Taxes.** Deferred income taxes are reported for temporary differences between items of income or expense reported in the financial statements and those reported for income tax purposes. Deferred taxes are computed using the asset and liability approach as prescribed in SFAS No. 109, Accounting for Income Taxes. Under this method, a deferred tax asset or liability is determined based on the enacted tax rates that will be in effect when the differences between the financial statement carrying amounts and tax basis of existing assets and liabilities are expected to be reported in an institution's income tax returns. The deferred tax provision for the year is equal to the net change in the net deferred tax asset from the beginning to the end of the year, less amounts applicable to the change in value related to investments available for sale. The effect on deferred taxes of a change in tax rates is recognized as income in the period that includes the enactment date. The primary differences between financial statement income and taxable income result from depreciation expense, mortgage servicing rights, loan loss reserves, deferred compensation, mark to market adjustments on our available for sale securities, and dividends received from the Federal Home Loan Bank of Seattle. Deferred income taxes do not include a liability for pre-1988 bad debt deductions allowed to thrift institutions that may be recaptured if the institution fails to qualify as a bank for income tax purposes in the future.

Comparison of Financial Condition at December 31, 2008 and September 30, 2008

Assets. For the three months ended December 31, 2008, total assets decreased \$6.9 million. The increases and decreases were primarily concentrated in the following asset categories:

|  | Balance at | Balance at | Increase (decrease) |         |
|--|------------|------------|---------------------|---------|
|  |            |            | Amount              | Percent |

Edgar Filing: Home Federal Bancorp, Inc. - Form 10-Q

|  | December<br>31,<br>2008 | September<br>30,<br>2008 | (dollars in thousands) |         |
|--|-------------------------|--------------------------|------------------------|---------|
| Cash and amounts due from<br>depository institutions | \$ 17,412               | \$ 23,270                | \$(5,858)              | (25.2)% |
| Mortgage-backed securities, at<br>fair value         | 188,237                 | 188,787                  | (550)                  | (0.3)   |
| Loans receivable, net                                | 466,169                 | 459,813                  | 6,356                  | 1.4     |

Cash and amounts due from depository institutions decreased \$5.9 million to \$17.4 million at December 31, 2008, from \$23.3 million at September 30, 2008. The decrease was primarily attributable to excess cash being used to pay off maturing borrowings from the Federal Home Loan Bank of Seattle (the "FHLB").

Securities. The fair value of mortgage-backed securities was virtually unchanged at \$188.2 million at December 31, 2008, compared to \$188.8 million at September 30, 2008. This was due to the significant increase in the value of the mortgage-backed securities portfolio as market interest rates declined and spreads on mortgage securities narrowed during the quarter first quarter of fiscal 2009. At December 31, 2008, the unrealized gain on the portfolio was \$2.9 million compared to an unrealized loss of \$2.3 million at September 30, 2008. This increase in the value of the securities portfolio nearly offset the reduction in outstanding balances from repayments of \$6.2 million. Principal reductions of mortgage-backed securities were higher in the first quarter of fiscal 2009 compared to the first quarter of fiscal 2008 as mortgage rates were significantly lower in the current year, increasing the number of mortgage loan refinancings in the first quarter of fiscal 2009.

Nearly all of the Company's mortgage-backed securities are issued by U.S. Government sponsored enterprises, primarily Fannie Mae and Freddie Mac. While the U.S. Government has recently affirmed its support for government sponsored enterprises and the mortgage-backed securities they issued, significant deterioration in the financial strength of Fannie Mae, Freddie Mac or mortgage-backed security insurers may have a material effect on the valuation and performance of the Company's mortgage-backed securities portfolio in future periods.

Non-agency, also referred to as "private label," mortgage-backed securities had a fair value of \$2.5 million at December 31, 2008, compared to their amortized cost of \$3.4 million. The securities carried a rating of 'AAA' by Moody's and Standard & Poor's at that date. The value of private label mortgage-backed securities have fallen and have been more volatile than securities issued by government-sponsored enterprises due to the deterioration of the national residential loan market. Management has reviewed the delinquency status and average collateral coverage of the loans pooled in the private label securities portfolio and has concluded the securities were not other than temporarily impaired at December 31, 2008. However, continued deterioration in the economy and rapid increases in unemployment may result in a change in the performance expectation for these securities in the future, which may negatively impact the Company's earnings.

At December 31, 2008, the Company did not own collateralized debt obligations or trust preferred securities.

FHLB Stock. At December 31, 2008, the Bank held \$9.6 million of common stock in the FHLB of Seattle. This security is reported at par value, which represents the Bank's cost. The FHLB of Seattle recently announced that it would report a risk-based capital deficiency under the regulations of the Federal Housing Finance Agency (the "FHFA"), its primary regulator, as of December 31, 2008, and as a result would not pay a dividend for the fourth calendar quarter of 2008 and that it would suspend the repurchase and redemption of outstanding common stock.

The FHLB of Seattle has communicated to the Company that they believe the calculation of risk-based capital under the current rules of the FHFA significantly overstates the market risk of the FHLB's private-label mortgage-backed securities in the current market environment and that they have enough capital to cover the risks reflected in the FHLB's balance sheet. As a result, the Company has not recorded an "other than temporary impairment" on its investment in FHLB stock. However, continued deterioration in the FHLB of Seattle's financial position may result in impairment in the value of those securities, the requirement that the Bank contribute additional funds to recapitalize the FHLB of Seattle, or reduce the Bank's ability to borrow funds from the FHLB of Seattle, impairing the Bank's ability to meet liquidity demands.

Loans. Net loans receivable increased \$6.4 million to \$466.2 million at December 31, 2008, from \$459.8 million at September 30, 2008. One- to four-family residential mortgage loans decreased \$7.0 million as the Company sold a majority of the one-to four-family loans that were originated. Consumer loans increased \$560,000 to \$56.8 million as

of December 31, 2008. Consistent with the Company's strategic plan, commercial, multifamily and acquisition and development loans increased \$16.3 million to \$214.9 million at December 31, 2008 from \$198.6 million at September 30, 2008.

Loans delinquent 30 to 89 days, which included \$4.5 million of loans on nonaccrual status, totaled \$10.7 million at December 31, 2008, compared to \$6.5 million at September 30, 2008, and \$5.3 million at December 31, 2007. Non-

Edgar Filing: Home Federal Bancorp, Inc. - Form 10-Q

performing assets, which includes all loans on nonaccrual status, impaired loans and other real estate owned, totaled \$18.4 million at December 31, 2008, compared to \$10.6 million at September 30, 2008, and \$2.3 million at December 31, 2007. The allowance for loan losses was \$8.0 million, or 1.69%, of gross loans at December 31, 2008, compared to \$4.6 million, or 0.98% of gross loans at September 30, 2008, and \$3.0 million, or 0.63% of gross loans at December 31, 2007.

The following table summarizes loans delinquent 30 to 89 days at December 31, 2008, and September 30, 2008:

|   | December<br>31,<br>2008 | September<br>30,<br>2008 |
|---|-------------------------|--------------------------|
|   | (in thousands)          |                          |
| Land acquisition and development            | \$ 2,268                | \$1,150                  |
| One- to four-family construction            | 1,376                   | 241                      |
| Commercial real estate                      | 2,313                   | 3,094                    |
| One- to four-family residential             | 4,545                   | 1,836                    |
| Other                                       | 188                     | 190                      |
| <b>Total loans delinquent 30 to 89 days</b> | <b>\$10,690</b>         | <b>\$6,511</b>           |

When a loan becomes 90 days delinquent, the Bank places the loan on nonaccrual status. A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Generally, an impaired loan is also placed on nonaccrual status, regardless of delinquency. As a result, some loans that are not 90 days or more past due may be in nonaccrual status if it is considered impaired. The delinquency table above includes \$4.5 million of loans that have been placed on nonaccrual status at December 31, 2008, which are also included in the table below that summarizes total nonperforming loans (including nonaccrual and impaired loans) at December 31, 2008, and September 30, 2008:

|   | December 31, 2008 |                    | September 30, 2008 |                    |
|---|-------------------|--------------------|--------------------|--------------------|
|   | Balance           | L o s s<br>Reserve | Balance            | L o s s<br>Reserve |
|   | (in thousands)    |                    |                    |                    |
| Land acquisition and development        | \$ 4,330          | \$ 936             | \$3,975            | \$ 916             |
| One- to four-family construction        | 5,389             | 832                | 4,239              | 596                |
| Commercial real estate                  | 3,071             | 273                | -                  | -                  |
| One- to four-family residential         | 4,240             | 713                | 1,701              | 219                |
| Other                                   | 4                 | -                  | 30                 | 2                  |
| <b>Total nonperforming and impaired</b> | <b>\$17,034</b>   | <b>2,754</b>       | <b>\$9,945</b>     | <b>1,733</b>       |



|                      |         |         |
|----------------------|---------|---------|
| loans                |         |         |
| General loss reserve | 5,273   | 2,846   |
|                      | \$8,027 | \$4,579 |

The Treasure Valley economy continues to deteriorate as unemployment rose quickly during the quarter from 4.80% in September 2008 to an estimated 6.50% in December 2008. New home and commercial real estate construction has come to a standstill as excess inventory in the residential and commercial real estate markets continues to put stress on property values. The pending closure of retail locations as a result of reduced consumer spending will exacerbate the problem.

The Company is just beginning to place properties into foreclosure and sale and management believes the Treasure Valley is at the beginning of a downturn in the commercial real estate market. As a result of this uncertainty, management recorded a significant provision for loan losses during the quarter ended December 31, 2008, in order to increase the general reserve component of the allowance for loan losses. While the \$2.4 million provision for loan losses for the full fiscal year of 2008 and the \$3.6 million provision recorded during the first quarter of fiscal 2009 exceeds the level of net charge-offs during those periods, management believes such an increase in the allowance for loan losses is prudent and appropriate and that the allowance for loan losses reflects management's best estimate of probable, known and estimable losses inherent in the loan portfolio at December 31, 2008. However, additional

information may later come to management's attention, evidencing losses in excess of the amounts estimated, which may negatively affect earnings in the future.

Last year, management realigned the Credit Administration Department and appointed a Chief Credit Officer, reporting directly to the Chief Executive Officer, in anticipation of this environment. The Bank also recently hired a senior workout professional to increase the Credit Administration Department's resources.

Nearly all of the Company's loans are secured by collateral located in the Treasure Valley or southern Idaho. In 2005, the Bank purchased approximately \$38.8 million of residential real estate loans from Countrywide Financial, now Bank of America, who continues to service the loans. Balances on the portfolio totaled \$24.1 million at December 31, 2008. Approximately 91% of the portfolio balance is secured by properties outside of the state of Idaho and delinquencies and foreclosures are rising quickly in that portfolio. At December 31, 2008, loans in this portfolio that were delinquent over 30 days totaled \$2.2 million, or 9%, of the portfolio, including \$1.9 million of nonperforming loans that are reported in the table above. The total reserve allocated to loans in the Countrywide portfolio was \$1.3 million at December 31, 2008, or 5% of the balance outstanding on that date.

Deposits. Deposits increased \$4.5 million, or 1.2%, to \$377.4 million at December 31, 2008, from \$372.9 million at September 30, 2008, primarily as a result of interest-bearing demand deposits. The increase in interest-bearing demand deposits was primarily attributed to growth in money market accounts as the Bank continued its emphasis on deposit products associated with a full-service commercial bank. The decrease in certificates of deposit was due to choosing not to match rates offered by local competitors that in many cases exceeded the Bank's cost of alternative funding sources. The Bank had no brokered deposits at December 31, 2008, or September 30, 2008. The following table details the composition of the deposit portfolio and changes in deposit balances:

|                                     | Balance<br>at<br>December<br>31,<br>2008 | Balance at<br>September<br>30,<br>2008 | Increase (decrease)    |         |
|-------------------------------------|--|--|------------------------|---------|
|                                     |  |  | Amount                 | Percent |
|                                     |  |  | (dollars in thousands) |         |
| Noninterest-bearing demand deposits | \$ 41,187                                | \$ 41,398                              | \$ (211)               | (0.5)%  |
| Interest-bearing demand deposits    | 134,148                                  | 127,714                                | 6,434                  | 5.0     |
| Savings deposits                    | 27,589                                   | 26,409                                 | 1,180                  | 4.5     |
| Certificates of deposit             | 174,475                                  | 177,404                                | (2,929)                | (1.7)   |
| Total deposit accounts              | \$377,399                                | \$372,925                              | \$4,474                | 1.2%    |

Approximately 76% of the certificates of deposit portfolio at December 31, 2008, are scheduled to mature within 12 months. While this presents an opportunity to reduce the cost of interest bearing deposits in the current low interest rate environment, the significant level of maturities of certificates also places a burden on the Company's liquidity if management is unable to retain the maturing balances.

Borrowings. FHLB advances decreased \$12.4 million, or 9.1%, to \$124.6 million at December 31, 2008, from \$137.0 million at September 30, 2008. We used excess cash and principal payment proceeds from our mortgage-backed securities and residential loan portfolios to reduce our advances as they matured. The Bank uses FHLB advances as an alternative funding source to deposits, manage funding costs, reduce interest rate risk, and to leverage the balance

sheet.

Deferred Income Tax Asset/Liability. The Company had a deferred tax asset of \$1.8 million at September 30, 2008 versus a deferred tax liability of \$310,000 at December 31, 2008. This change primarily resulted from a shift from an unrealized loss on the Company's mortgage-backed securities' portfolio as of September 30, 2008 to an unrealized gain as of December 31, 2008, as interest rates fell and spreads narrowed, increasing the value of the securities portfolio during the quarter.

Equity. Stockholders' equity increased \$2.3 million, or 1.1%, to \$207.4 million at December 31, 2008, from \$205.2 million at September 30, 2008. Significant activity among equity accounts over the past three months include the

allocation of earned ESOP shares, equity compensation and the exercise of stock options totaling \$835,000, and a \$3.1 million increase in the value of securities available for sale, net of taxes, offset by a net loss for the quarter of \$801,000 and \$893,000 in cash dividends paid to stockholders.

#### Comparison of Operating Results for the Three Months Ended December 31, 2008, and December 31, 2007

Net loss for the three months ended December 31, 2008 was \$801,000, or \$0.05 per diluted share, compared to net income of \$947,000, or \$0.06 per diluted share, for the three months ended December 31, 2007. Earnings per share for the prior period have been adjusted to reflect the impact of the Conversion and reorganization of the Company. Total revenue for the quarter ended December 31, 2008, which consisted of net interest income before the provision for loan losses plus noninterest income, increased \$525,000, or 7%, to \$8.2 million, compared to \$7.7 million for the quarter ended December 31, 2007. However, total revenue for the first quarter of fiscal 2009 declined \$344,000, or 4%, from the linked fourth quarter of fiscal 2008. The Company's efficiency ratio improved to 73.5% for the quarter ended December 31, 2008, compared to 76.6% for the same quarter a year ago as an increase in net interest income outpaced slowing service charge and fee income coupled with a slight increase in noninterest expenses.

**Net Interest Income.** Net interest income increased \$689,000, or 13.6%, to \$5.7 million for the three months ended December 31, 2008, from \$5.1 million for the three months ended December 31, 2007. The increase in net interest income is primarily attributable to a decrease in interest expense. Current rates paid on deposits are significantly lower than in the prior year. In addition, Federal Home Loan Bank borrowing balances are lower than in the same period of the prior year as maturing advances have been repaid with excess liquidity.

The Company's net interest margin increased 40 basis points to 3.37% for the quarter ended December 31, 2008, from 2.97% for the same quarter last year. The improvement in the net interest margin is primarily attributable to the increase in interest earning assets that resulted from the proceeds of the Company's second step conversion and stock offering completed on December 19, 2007, while the increase in net interest income is attributable to decreases in interest expense also contributed to the increase in the margin in 2008.

The following table sets forth the impacts to the Company's net interest income from changes in balances of interest earning assets and interest bearing liabilities as well as changes in interest rates. The rate column shows the effects attributable to changes in rate (changes in rate multiplied by prior volume). The volume column shows the effects attributable to changes in volume (changes in volume multiplied by prior rate). Changes attributable to both rate and volume, which cannot be segregated, are allocated proportionately to the changes in rate and volume.

Edgar Filing: Home Federal Bancorp, Inc. - Form 10-Q

|   | Three Months Ended December 31,<br>2008             |                |           |
|---|---|----------------|-----------|
|   | Compared to Three Months Ended<br>December 31, 2007 |                |           |
|   | Increase (Decrease)                                 |                |           |
|   | Due to  |                |           |
|   | Rate  | Volume         | Total     |
|   |   | (in thousands) |           |
| Interest-earning assets:                                    |   |                |           |
| Loans receivable, net                                       | \$(772)   | \$(178)        | \$ (950)  |
| Loans held for sale   | (3)   | (10)           | (13)      |
| Investment securities, including interest-                  |   |                |           |
| bearing deposits in other banks                             | (127)   | (94)           | (221)     |
| Mortgage-backed securities                                  | (35)  | 297            | 262       |
| FHLB stock  | (52)  | -              | (52)      |
| Total net change in income on interest-earning assets       | \$(989)   | \$ 15          | \$ (974)  |
| Interest-bearing liabilities:                               |   |                |           |
| Savings deposits  | \$ 11   | \$ 9           | \$ 20     |
| Interest-bearing demand deposits                            | (42)  | -              | (42)      |
| Money market accounts                                       | (289)   | 30             | (259)     |
| Certificates of deposit                                     | (517)   | (398)          | (915)     |
| Total deposits  | (837)   | (359)          | (1,196)   |
| FHLB advances   | 48  | (515)          | (467)     |
| Total net change in expense on interest-bearing liabilities | \$(789)   | \$(874)        | \$(1,663) |
| Total increase in net interest income                       |   |                | \$ 689    |

Interest and Dividend Income. Total interest and dividend income for the three months ended December 31, 2008, decreased \$974,000, or 9.5%, to \$9.3 million, from \$10.3 million for the three months ended December 31, 2007. The decrease during the quarter was primarily attributable to a decrease on yields earned on interest earning assets.

The following table compares detailed average earning asset balances, associated yields, and resulting changes in interest and dividend income:

|  | Three Months Ended December 31, |       |         |       |            |
|--|---------------------------------|-------|---------|-------|------------|
|  | 2008                            |       | 2007    |       |            |
|  | Average                         | Yield | Average | Yield | Increase/  |
|  | Balance                         |       | Balance |       | (Decrease) |
|  |                                 |       |         |       | in         |
|  |                                 |       |         |       | Interest   |
|  |                                 |       |         |       | and        |
|  |                                 |       |         |       | Dividend   |

Income  
from  
2007

(dollars in thousands)

|  |           |        |           |       |         |
|--|-----------|--------|-----------|-------|---------|
| Interest-bearing deposits in other banks | \$ 12,207 | 1.41%  | \$ 24,429 | 4.32% | \$(221) |
| Mortgage-backed securities               | 185,666   | 4.75   | 160,705   | 4.84  | 262     |
| Loans receivable, net                    | 471,888   | 6.00   | 482,780   | 6.66  | (950)   |
| Loans held for sale                      | 2,022     | 5.76   | 2,675     | 6.25  | (13)    |
| FHLB stock                               | 9,591     | (1.38) | 9,591     | 0.79  | (52)    |
| Total interest-earning assets            | \$681,374 | 5.48%  | \$680,180 | 6.06% | \$(974) |

The decline in the yield on interest-bearing deposits in other banks reflects the significantly lower short-term interest rate environment in the first quarter of fiscal 2009 compared to the first quarter of fiscal 2008. Mortgage-backed securities were purchased during the first quarter of last fiscal year using proceeds from the Conversion at yields lower than the portfolio average, thereby comparatively reducing the overall yield in the first quarter of 2009.

The yield on loans fell to 6.00% in the first quarter of 2009 as a result of the decrease in the Wall Street Journal Prime rate from 4.00% at the beginning of the quarter to 3.25% at the end of the quarter. The Prime rate averaged 7.65% during the same quarter last year. Additionally, the significant increase in loans on nonaccrual status during the first quarter of 2009 reduced interest income by approximately \$90,000.

As discussed earlier, the FHLB of Seattle announced during the first quarter of fiscal 2009 that they would not pay a dividend to shareholders for the quarter ended September 30, 2008. As a result, the Bank reversed the accrued dividend during the quarter ended December 31, 2008, resulting in a negative effective yield.

Interest Expense. Interest expense decreased \$1.7 million, or 31.7%, to \$3.6 million for the three months ended December 31, 2008 from \$5.2 million for the three months ended December 31, 2007. The average balance of total interest-bearing liabilities decreased \$72.5 million, or 13.4%, to \$470.3 million for the three months ended December 31, 2008 from \$542.8 million for the three months ended December 31, 2007. The decrease in interest expense in 2008 was mainly due to reductions in the outstanding balances of FHLB advances and certificates of deposit, as well as a significantly lower interest rate environment in the first quarter of fiscal 2009 compared to the first quarter of fiscal 2008.

The following table details average balances, cost of funds and the change in interest expense:

|                                    | Three Months Ended December 31, |       |                    |       | Increase/<br>(Decrease)<br>in Interest<br>Expense<br>from<br>2007 |
|------------------------------------|---------------------------------|-------|--------------------|-------|---|
|                                    | 2008                            |       | 2007               |       |   |
|                                    | Average<br>Balance              | Cost  | Average<br>Balance | Cost  |   |
| (dollars in thousands)             |                                 |       |                    |       |   |
| Savings deposits                   | \$ 27,294                       | 0.84% | \$ 22,607          | 0.65% | \$ 20   |
| Interest-bearing demand deposits   | 77,609                          | 0.55  | 77,847             | 0.77  | (42)  |
| Money market deposits              | 55,268                          | 1.45  | 51,641             | 3.56  | (259)   |
| Certificates of deposit            | 177,219                         | 3.73  | 213,930            | 4.80  | (915)   |
| FHLB advances                      | 132,929                         | 4.71  | 176,794            | 4.60  | (467)   |
| Total interest-bearing liabilities | \$470,319                       | 3.05% | \$542,819          | 3.87% | \$(1,663)   |

The cost of savings deposits increased due to product disintermediation during the first quarter of 2009 as customers shifted their balances to a higher-yielding savings product. The decline in the cost of all other interest-bearing deposits reflects the significantly lower interest rate environment in fiscal 2009 compared to the first quarter of fiscal 2008. The cost of FHLB advances increased as advances maturing during the quarter ended December 31, 2008, carried a lower average rate than the portfolio average.

Provision for Loan Losses. A provision for loan losses of \$3.6 million was established in connection with an analysis of the loan portfolio for the quarter ended December 31, 2008, compared to a provision for loan losses of \$287,000 for

the same quarter of the prior year. The increase in the provision reflects the increase in nonperforming loans during the three months ended December 31, 2008, and the high level of economic uncertainty in the Treasure Valley. Management increased the specific allocation of the allowance for loan losses for some impaired loans. Additionally, the estimated loss rates and the range of losses were increased during the quarter ended December 31, 2008, as the Treasure Valley and national economies continued to deteriorate rapidly.

While management believes the estimates and assumptions used in its determination of the adequacy of the allowance are reasonable, there can be no assurance that such estimates and assumptions will not be proven incorrect in the future, or that the actual amount of future provisions will not exceed the amount of past provisions or



that any increased provision that may be required will not adversely impact the Company's financial condition and results of operations. In addition, the determination of the amount of the allowance for loan losses is subject to review by bank regulators, as part of the routine examination process, which may result in the establishment of additional reserves based upon their judgment of information available to them at the time of their examination.

Standard provisions for loan losses are established based upon the type of loan and the risk factors associated with that loan type. As the Bank increases its commercial loan portfolio, the Bank anticipates it will increase its allowance for loan losses based upon the higher risk characteristics associated with commercial loans compared with one- to four-family residential loans, which have historically comprised the majority of the Bank's loan portfolio.

The following table details selected activity associated with the allowance for loan losses:

|   | At or For the Three Months<br>Ended December 31, |           |
|---|--|-----------|
|   | 2008   | 2007      |
|   | (dollars in thousands)                           |           |
| Provision for loan losses   | \$ 3,575   | \$ 287    |
| Net charge-offs   | 127  | 260       |
| Allowance for loan losses   | 8,027  | 3,015     |
| Allowance for loan losses as a percentage of gross loans<br>receivable                        | 1.69%  | 0.63%     |
| Nonperforming loans   | \$ 17,034  | \$ 1,656  |
| Allowance for loan losses as a percentage of<br>nonperforming loans                           | 47.12%   | 182.07%   |
| Nonaccrual and 90 days or more past due loans as a<br>percentage of gross loans<br>receivable | 3.58   | 0.34      |
| Loans receivable, net   | \$466,169  | \$477,446 |

Noninterest Income. Noninterest income decreased \$164,000, or 6.3%, to \$2.5 million for the three months ended December 31, 2008 from \$2.6 million for the three months ended December 31, 2007. The decrease was primarily attributable to a \$123,000 decrease in service charges and fees, reflecting the continuing slowdown in consumer spending and the resulting decline in the number of checking and debit card transactions.

The following table provides a detailed analysis of the changes in components of noninterest income:

|  | Three Months Ended     |         | Increase (decrease) |         |
|--|------------------------|---------|---------------------|---------|
|  | 2008                   | 2007    | Amount              | Percent |
|  | (dollars in thousands) |         |                     |         |
| Service fees and<br>charges  | \$2,109                | \$2,232 | \$(123)             | (5.5)%  |
| Gain on sale of loans  | 190                    | 185     | 5                   | 2.7     |
| Increase in cash<br>surrender value<br>of bank owned life<br>insurance | 106                    | 104     | 2                   | 1.9     |
| Loan servicing fees  | 69                     | 127     | (58))               | (45.7)  |
| Mortgage servicing<br>rights, net                                      | (31)                   | (68)    | 37                  | 54.4    |

Edgar Filing: Home Federal Bancorp, Inc. - Form 10-Q

|                   |         |         |         |        |
|-------------------|---------|---------|---------|--------|
| Other             | 18      | 45      | (27)    | (60.0) |
| Total noninterest |         |         | \$(164) |        |
| income            | \$2,461 | \$2,625 | )       | (6.3)% |

Noninterest Expense. Noninterest expense increased \$151,000, or 2.6%, to \$6.0 million for the three months ended December 31, 2008 from \$5.9 million for the three months ended December 31, 2007. The following table provides a detailed analysis of the changes in components of noninterest expense:

|                           | Three Months Ended   |         | Increase (decrease)    |         |
|---------------------------|----------------------|---------|------------------------|---------|
|                           | December 31,<br>2008 | 2007    | Amount                 | Percent |
|                           |                      |         | (dollars in thousands) |         |
| Compensation and benefits | \$3,575              | \$3,699 | \$(124)                | (3.4)%  |
| Occupancy and equipment   | 770                  | 711     | 59                     | 8.3     |
| Data processing           | 542                  | 522     | 20                     | 3.8     |
| Advertising               | 248                  | 287     | (39)                   | (13.6)  |
| Other                     | 899                  | 664     | 235                    | 35.4    |
| Total noninterest expense | \$6,034              | \$5,883 | \$ 151                 | 2.6%    |

Compensation and benefits declined 3.4% in the first quarter of 2009 compared to the year-ago period primarily due to the absence of an accrual for incentive compensation during the quarter ended December 31, 2008, and a reduction in retirement benefit expense in the current quarter. Occupancy and equipment expense was higher in the first quarter of fiscal 2009 as the Bank opened two stand-alone banking offices during fiscal 2008.

The increase in other noninterest expense in the first quarter of 2009 includes increases in professional fees related to the Company's fiscal year end, which was September 30, 2008, and legal expenses related to foreclosures and the workout of troubled loans. Additionally, Federal Deposit Insurance Corporation premiums were higher in the first quarter of fiscal 2009 as the Company was able to apply some credits to the assessment in 2008. Additionally, management expects deposit insurance premiums to increase further during fiscal 2009 as a result of recent FDIC-imposed increases in the assessment rates, which are scheduled to commence during the Company's second quarter of fiscal 2009.

Income Tax Expense (Benefit). The Company recorded an income tax benefit of \$(602,000) for the three months ended December 31, 2008. Net loss before income taxes was (\$1.4) million for the three months ended December 31, 2008 compared to net income of \$1.5 million for the three months ended December 31, 2007.

#### Liquidity, Commitments and Capital Resources

**Liquidity.** The Company actively analyzes and manages the Bank's liquidity with the objectives of maintaining an adequate level of liquidity and to ensure the availability of sufficient cash flows to support loan growth, fund deposit withdrawals, fund operations and satisfy other financial commitments. See the "Consolidated Statements of Cash Flows" contained in Item 1 - Financial Statements, included herein.

The primary sources of funds are customer deposits, loan repayments, loan sales, maturing investment securities, and FHLB advances. These sources of funds are used to make loans, acquire investment securities and other assets, and fund continuing operations. While maturities and the scheduled amortization of loans are a predictable source of funds, deposit flows and mortgage prepayments are greatly influenced by the level of interest rates, economic conditions and competition. Management believes that the Company's current liquidity position and forecasted operating results are sufficient to fund all of the Bank's existing commitments.

Liquidity is essential to the Company's business. An inability to raise funds through deposits, borrowings, the sale of loans and other sources could have a substantial negative effect on liquidity. The Company's access to funding sources

in amounts adequate to finance the Bank's activities on acceptable terms could be impaired by factors that affect the Company and the Bank specifically or within the financial services industry or economy in general. Factors that could detrimentally impact the Company's access to liquidity sources include adverse regulatory action against us, a disruption in the financial markets or negative views and expectations about the prospects for the financial services industry in light of the recent turmoil faced by banking organizations and the continued deterioration in credit markets.

At December 31, 2008, certificates of deposit amounted to \$174.5 million, or 46.2% of total deposits, including \$123.5 million that are scheduled to mature by December 31, 2009. Historically, the Bank has been able to retain a significant amount of deposits as they mature. However, recent disruptions in the credit markets have resulted in a highly price-competitive market for certificates of deposit. These rates currently exceed alternative costs of borrowings and are high compared to historical spreads to U.S. Treasury note rates. Additionally, since loan demand continues to slow, Management has been reluctant to offer rates in excess of wholesale borrowing costs. This has resulted in some deposit runoff as customers are moving their maturing balances to competitors at a higher pace than the Bank has historically experienced.

At December 31, 2008, the Bank maintained a line of credit with the FHLB of Seattle equal to 40% of total assets to the extent the Bank provides qualifying collateral and holds sufficient FHLB stock. At December 31, 2008, the Bank was in compliance with the collateral requirements and \$149.0 million of the line of credit was available. The Bank is highly dependent on the FHLB of Seattle to provide the primary source of wholesale funding for immediate liquidity and borrowing needs. The failure of the FHLB of Seattle or the FHLB system in general, may materially impair the Company's ability to meet our growth plans or to meet short and long term liquidity demands. However, the Company's mortgage backed securities are marketable and could be sold to obtain cash to meet liquidity demands should access to FHLB funding be impaired. Additionally, the Bank could access funding from its correspondent bank through a federal funds line of credit, the Discount Window at the Federal Reserve Bank of San Francisco or through the origination of out of market brokered deposits.

Off-Balance Sheet Arrangements. The Bank is party to financial instruments with off-balance sheet risk in the normal course of business in order to meet the financing needs of the Bank's customers. These financial instruments generally include commitments to originate mortgage, commercial and consumer loans, and involve to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet. The Bank's maximum exposure to credit loss in the event of nonperformance by the borrower is represented by the contractual amount of those instruments. Because some commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The same credit policies are used in making commitments as are used for on-balance sheet instruments. Collateral is required in instances where deemed necessary.

Undisbursed balances of loans closed include funds not disbursed but committed for construction projects. Unused lines of credit include funds not disbursed, but committed for, home equity, commercial and consumer lines of credit.

Commercial letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. Those guarantees are primarily used to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

The following is a summary of commitments and contingent liabilities with off-balance sheet risks as of December 31, 2008:

|  | Contract or<br>Notional<br>Amount<br>(in<br>thousands) |
|--|--|
| Commitments to originate loans:        |  |
| Fixed rate                             | \$11,385   |
| Adjustable rate                        | 5,505  |
| Undisbursed balance of loans<br>closed | 9,883  |
| Unused lines of credit                 | 40,704   |
| Commercial letters of credit           | 829  |
| Total                                  | \$68,306   |

Capital. Consistent with the Bank's goal to operate a sound and profitable financial organization, efforts are ongoing to actively seek to maintain a "well capitalized" institution in accordance with regulatory standards. The Bank's total regulatory capital was \$140.8 million at December 31, 2008, or 20.6%, of total assets on that date. As of December 31, 2008, the Bank exceeded all regulatory capital requirements. The Bank's regulatory capital ratios at December 31, 2008 were as follows: Tier 1 capital 20.6%; Tier 1 (core) risk-based capital 30.0%; and total risk-based capital 31.3%. The applicable regulatory capital requirements to be considered well capitalized are 5%, 6% and 10%, respectively.

### Item 3. Quantitative and Qualitative Disclosures about Market Risk

The Company's Board of Directors has established an asset and liability management policy to guide management in maximizing net interest spread by managing the differences in terms between interest-earning assets and interest-bearing liabilities while maintaining acceptable levels of liquidity, capital adequacy, interest rate sensitivity, credit risk and profitability. The Asset/Liability Management Committee, consisting of certain members of senior management, communicate, coordinate and manage asset/liability positions consistent with the business plan and Board-approved policies, as well as to price savings and lending products, and to develop new products.

One of the Bank's primary financial objectives is to generate ongoing profitability. The Bank's profitability depends primarily on its net interest income, which is the difference between the income it receives on its loan and investment portfolio and its cost of funds, which consists of interest paid on deposits and borrowings. The rates the Company earns on assets and pays on liabilities generally are established contractually for a period of time. Market interest rates change over time. The Bank's loans generally have longer maturities than the deposits. Accordingly, the Company's results of operations, like those of other financial institutions, are affected by changes in interest rates and the interest rate sensitivity of assets and liabilities. The Bank measures its interest rate sensitivity on a quarterly basis using an internal model.

Management employs various strategies to manage the Company's interest rate sensitivity including: (1) selling long-term fixed-rate mortgage loans in the secondary market; (2) borrowing intermediate to long-term funds at fixed rates from the FHLB; (3) originating commercial and consumer loans at shorter maturities or at variable rates; (4) originating adjustable rate mortgage loans; (5) appropriately modifying loan and deposit pricing to capitalize on the then current market opportunities; and (6) increasing lower cost core deposits, such as savings and checking accounts. At December 31, 2008, the Company had no off-balance sheet derivative financial instruments, and the Bank did not

maintain a trading account for any class of financial instruments or engage in hedging activities or purchase high risk derivative instruments. Furthermore, the Company is not subject to foreign currency exchange rate risk or commodity price risk.

There has not been any material change in the market risk disclosures contained in the Company's 2008 Form 10-K.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures.

An evaluation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934 (the "Exchange Act")) was carried out under the supervision and with the participation of the Company's Chief Executive Officer, Chief Financial Officer, and other members of the Company's management team as of the end of the period covered by this quarterly report. The Company's Chief Executive Officer and Chief Financial Officer concluded that as of December 31, 2008, the Company's disclosure controls and procedures were effective in ensuring that the information required to be disclosed by the Company in the reports it files or submits under the Act is (i) accumulated and communicated to the Company's management (including the Chief Executive Officer and Chief Financial Officer) in a timely manner, and (ii) recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms.

(b) Changes in Internal Controls.

There have been no changes in the Company's internal control over financial reporting (as defined in 13a-15(f) of the Exchange Act) that occurred during the quarter ended December 31, 2008, that have materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting. A number of internal control procedures were, however, modified during the quarter in conjunction with the Bank's internal control testing. The Company also continued to implement suggestions from its internal auditor and independent auditors to strengthen existing controls.

The Company intends to continually review and evaluate the design and effectiveness of its disclosure controls and procedures and to improve its controls and procedures over time and to correct any deficiencies that it may discover in the future. The goal is to ensure that senior management has timely access to all material financial and non-financial information concerning the Company's business. While the Company believes the present design of its disclosure controls and procedures is effective to achieve its goal, future events affecting its business may cause the Company to modify its disclosure controls and procedures. The Company does not expect that its disclosure controls and procedures and internal control over financial reporting will prevent every error or instance of fraud. A control procedure, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control procedure are met. Because of the inherent limitations in all control procedures, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns in controls or procedures can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any control procedure is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control procedure, misstatements due to error or fraud may occur and not be detected.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

From time to time, the Company is engaged in legal proceedings in the ordinary course of business, none of which are currently considered to have a material impact on the Company's financial position or results of operations.



Item 1A. Risk Factors

Other than discussed in the following paragraph, we believe there have been no significant changes in risk factors compared to the factors identified in our 2008 Form 10-K.

---

25

The failure of the Federal Home Loan Bank (“FHLB”) of Seattle or the national Federal Home Loan Bank System may have a material negative impact on our earnings and liquidity.

Recently, the FHLB of Seattle announced that it did not meet minimum regulatory capital requirements for the quarter ended September 30, 2008, and that it did not expect to comply with those requirements at December 31, 2008, due to the deterioration in the market value of their mortgage-backed securities portfolio. As a result, the FHLB of Seattle cannot pay a dividend on their common stock and it cannot repurchase or redeem common stock. While the FHLB of Seattle has announced it does not anticipate that additional capital is immediately necessary, nor does it believe that its capital level is inadequate to support realized losses in the future, the FHLB of Seattle could require its members, including Home Federal Bank, to contribute additional capital in order to return the FHLB of Seattle to compliance with capital guidelines.

At December 31, 2008, we held \$9.6 million of common stock in the FHLB of Seattle. Should the FHLB of Seattle fail, we anticipate that our investment in the FHLB’s common stock would be “other than temporarily” impaired and may have no value.

At December 31, 2008, we held \$926,000 of cash on deposit with the FHLB of Seattle. At that date, all other cash and cash equivalents were held on deposit at the Federal Reserve Bank of San Francisco, or on hand in branch office vaults.

At December 31, 2008, we maintained a line of credit with the FHLB of Seattle equal to 40% of total assets to the extent Home Federal Bank provides qualifying collateral and holds sufficient FHLB stock. At December 31, 2008, we were in compliance with collateral requirements and \$149.0 million of the line of credit was available for additional borrowings. We are highly dependent on the FHLB of Seattle to provide the primary source of wholesale funding for immediate liquidity and borrowing needs. The failure of the FHLB of Seattle or the FHLB system in general, may materially impair our ability to meet our growth plans or to meet short and long term liquidity demands. However, our mortgage-backed securities are marketable and could be sold to obtain cash to meet liquidity demands should access to FHLB funding be impaired. Additionally, we could access funding from our correspondent bank through a federal funds line of credit, the Discount Window at the Federal Reserve Bank of San Francisco or through the origination of out of market brokered deposits.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(a) Not applicable.

(b) Not applicable.

(c) Stock Repurchases. On December 23, 2008, the Company’s Board of Directors approved a 5% share repurchase program, which authorized management to repurchase up to 867,970 shares of the Company’s outstanding common stock. No shares were repurchased between October 1, 2008, and December 31, 2008.

## Item 3. Defaults Upon Senior Securities

Not applicable.

## Item 4. Submission of Matters to a Vote of Security Holders

Not applicable.

Item 5. Other Information

Not applicable.

Item 6. Exhibits

- 2.1 Plan of Conversion and Reorganization (1)
- 3.1 Articles of Incorporation of the Registrant (2)
- 3.2 Bylaws of the Registrant (2)
- 10.1 Amended Employment Agreement entered into by Home Federal Bank with Len E. Williams (9)
- 10.2 Employment Agreement entered into by Home Federal Bancorp, Inc. with Len E. Williams (9)
- 10.3 Amended Employment Agreement entered into by Home Federal Bank with Daniel L. Stevens (9)
- 10.4 Amended Employment Agreement entered into by Home Federal Bancorp, Inc. with Daniel L. Stevens (9)
- 10.5 Form of Amended Severance Agreement for Executive Officers (7)
- 10.6 Form of Amended Severance Agreement for new Executive Officers (7)
- 10.7 Form of Home Federal Bank Employee Severance Compensation Plan \*
- 10.8 Form of Director Indexed Retirement Agreement entered into by Home Federal Savings and Loan Association of Nampa with each of its Directors (2)
- 10.9 Form of Director Deferred Incentive Agreement entered into by Home Federal Savings and Loan Association of Nampa with each of its Directors (2)
- 10.10 Form of Split Dollar Agreement entered into by Home Federal Savings and Loan Association of Nampa with Daniel L. Stevens, N. Charles Hedemark, Fred H. Helpenstell, M.D., Richard J. Schrandt, James R. Stamey and Robert A. Tinstman (2)
- 10.11 Form of Executive Deferred Incentive Agreement, and amendment thereto, entered into by Home Federal Savings and Loan Association of Nampa with Daniel L. Stevens, Robert A. Schoelkoph, and Lynn A. Sander (2)
- 10.12 Form of Amended and Restated Salary Continuation Agreement entered into by Home Federal Savings and Loan Association of Nampa with Daniel L. Stevens, Len E. Williams, Steven E. Emerson, Robert A. Schoelkoph, and Lynn A. Sander (2)
- 10.13 2005 Stock Option and Incentive Plan approved by stockholders on June 23, 2005 and Form of Incentive Stock Option Agreement and Non-Qualified Stock Option Agreement (3)
- 10.14 2005 Recognition and Retention Plan approved by stockholders on June 23, 2005 and Form of Award Agreement (3)
- 10.15 Form of new Director Retirement Plan entered into by Home Federal Bank with each of its Directors (4)
- 10.16 Transition Agreement with Daniel L. Stevens (5)
- 10.17 Agreement Regarding Terms of Employment Offer with Steven K. Eyre (6)
- 10.18 Agreement Regarding Terms of Employment Offer with Eric S. Nadeau (8)
- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act \*

31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act \*

32 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act \*

- 
- (1) Filed as an exhibit to the Registrant's Current Report on Form 8-K dated May 11, 2007.
  - (2) Filed as an exhibit to the Registrant's Registration Statement on Form S-1 (333-146289).
  - (3) Filed as an exhibit to the Registrant's Registration Statement on Form S-8 (333-127858).
  - (4) Filed as an exhibit to the Registrant's Current Report on Form 8-K dated October 21, 2005.
  - (5) Filed as an exhibit to the Registrant's Current Report on Form 8-K dated August 21, 2006.
  - (6) Filed as an exhibit to the Registrant's Current Report on Form 8-K dated November 15, 2007.
  - (7) Filed as an exhibit to the Registrant's Quarterly Report on Form 10-Q for the quarter ended December 31, 2007.
  - (8) Filed as an exhibit to the Registrant's Current Report on Form 8-K dated May 15, 2008.
  - (9) Filed as an exhibit to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2008

\* Filed herewith

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Home Federal Bancorp, Inc.

Date: February 6, 2009

/s/ Len E. Williams  
Len E. Williams

President and  
Chief Executive Officer  
(Principal Executive Officer)

Date: February 6, 2009  
S. Nadeau

/s/ Eric

Eric S. Nadeau  
Executive Vice President and  
Chief Financial Officer  
(Principal Financial and Accounting Officer)

EXHIBIT INDEX

|      |  |
|------|--|
| 10.7 | Form of Home Federal Bank Employee Severance Compensation Plan                             |
| 31.1 | Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act |
| 31.2 | Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act |
| 32   | Certification Pursuant to Section 906 of the Sarbanes-Oxley Act                            |

---